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No. 96-686

In the Supreme Court of the United States

OCTOBER TERM, 1996

AMOCO ENERGY TRADING CORP., ET AL., PETITIONERS

v.

FEDERAL ENERGY REGULATORY COMMISSION, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION IN OPPOSITION

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QUESTION PRESENTED

Whether the Federal Energy Regulatory Commission correctly determined that it lacks jurisdiction under the Natural Gas Act, 15 U.S.C. 717 *et seq.*, over the natural gas gathering rates charged by a natural gas company's affiliate, when the affiliate performs its gathering services independent of, and at arms length from, the natural gas company's interstate transportation services.

TABLE OF CONTENTS

	Page
Opinions below	1
Jurisdiction	1
Statement	2
Argument	9
Conclusion	13

TABLE OF AUTHORITIES

Cases:

Altamont Gas Transmission Co. v. *FERC*, 92 F.2d 1239 (D.C. Cir. 1996)	12
Amerada Hess Corp., 52 F.E.R.C. ¶ 61,268 (1990)	2
Chevron U.S.A. Inc. v. *NRDC, Inc.*, 467 U.S. 837 (1984)	7
Colorado Interstate Gas Co., Inc. v. *FPC*, 324 U.S. 581 (1945)	3, 7, 10
Interstate Natural Gas Co. v. *FPC*, 331 U.S. 682 (1947)	7
KansOk Partnership, 73 F.E.R.C. ¶ 61,160, order granting stay, in part, 73 F.E.R.C. ¶ 61,293 (1995), clarified, 75 F.E.R.C. ¶ 61,265 (1996)	8, 11
Louisiana Gas System, Inc., 73 F.E.R.C. ¶ 61,161 (1995)	9, 11
Northern Natural Gas Co. v. *FERC*, 929 F.2d 1261 (8th Cir.), cert. denied, 502 U.S. 856 (1991)	2, 4, 7, 10, 11
Phillips Petroleum Co. v. *Wisconsin*, 347 U.S. 672 (1954)	3, 7
United Distrib. Co. v. *FERC*, 88 F.3d 1105 (D.C. Cir. 1996)	3

Statutes and regulations:

Natural Gas Act, 15 U.S.C. 717 *et seq.*:	
§ 1(b), 15 U.S.C. 717(b)	2, 5, 6, 7, 10
§ 2(6), 15 U.S.C. 717a(6)	3, 10

Statutes and regulations—Continued: Page

§ 4, 15 U.S.C. 717c 6, 8, 9
§ 4(a), 15 U.S.C. 717c(a) 3, 9, 10
§ 4(c), 15 U.S.C. 717c(c) 3
§ 4(e), 15 U.S.C. 717c(e) 3
§ 5, 15 U.S.C. 717d 6, 8, 9
§ 5(a), 15 U.S.C. 717d(a) 3
18 C.F.R.:
Section 284.8(a)(1) 4
Section 284.9(a)(1) 4

Miscellaneous:

FERC Order No. 636, 57 Fed. Reg. 13,267, on reh'g, Order No. 636-A, 57 Fed. Reg. 36,128 (1992), aff'd in part and remanded in part *sub nom. United States* v. *FERC*, 88 F.3d 1105 (D.C. Cir. 1996) 3

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1-33) as amended (Pet. App. 34-35) is reported at 90 F.3d 536. The opinions of the Federal Energy Regulatory Commission (Pet. App. 36-103, 104-170) are reported at 67 F.E.R.C. ¶ 61,257 and 69 F.E.R.C. ¶ 61,280.

JURISDICTION

The judgment of the court of appeals was entered on August 2, 1996. The petition for a writ of certiorari

was filed on October 31, 1996. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1.a. Section 1(b) of the Natural Gas Act of 1938 (NGA), 15 U.S.C. 717(b), states that the provisions of the Act "shall apply to the transportation of natural gas in interstate commerce, * * * the sale in interstate commerce of natural gas for resale, * * * and * * * natural-gas companies engaged in such transportation or sale," but not to the "production or gathering of natural gas." "Gathering" is "the process of collecting gas at the point of production (the wellhead) and moving it to a collection point for further movement through a pipeline's principal transmission system." *Northern Natural Gas Co.* v. *FERC*, 929 F.2d 1261, 1265 (8th Cir.), cert. denied, 502 U.S. 856 (1991). There is no bright-line test for determining whether an activity constitutes interstate transportation, which falls within the jurisdiction of the NGA, or gathering, which does not. The Federal Energy Regulatory Commission (Commission) makes that determination on a case-by-case basis, applying a "primary function" test. See *Amerada Hess Corp.*, 52 F.E.R.C. ¶ 61,268 (1990).[1]

Sections 4 and 5 of the NGA, 15 U.S.C. 717c and 717d, require the Commission to establish for natural

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[1] The "primary function" test involves consideration of various factors: (1) the length and diameter of the pipelines; (2) the extension of the facility beyond the central point in the field; (3) the pipelines' geographic configuration; (4) the location of compressors and processing plants; (5) the location of wells along all or part of the facility; and (6) the operating pressure of the pipelines. Pet. App. 11-13 & n.16. See, *e.g.*, *id.* at 46-54.

gas companies "just and reasonable rates" for or in connection with "the transportation or sale of natural gas subject to the jurisdiction of the Commission." 15 U.S.C. 717c(a) and 717d(a).[2] Section 4(c) requires natural gas companies to file their rates with the Commission, 15 U.S.C. 717c(c), and Sections 4(e) and 5(a) authorize the Commission to determine the lawfulness of any such rates or changes in rates, 15 U.S.C. 717c(e) and 717d(a).

b. Traditionally, interstate pipelines operated primarily as gas merchants, buying gas at the wellhead and selling it either to local distribution companies for resale or directly to end-users. Under that regime, pipelines charged a single "bundled" rate for both the gas sold and its transportation to the purchaser. In regulating the rate that an interstate pipeline could charge for the sale of gas, the Commission had jurisdiction to consider the costs of production or gathering that were embedded in the pipeline's sales rates. *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672, 677 (1954); *Colorado Interstate Gas Co.* v. *FPC*, 324 U.S. 581, 601-604 (1945).

Recently, after implementing a series of orders to foster a more competitive marketplace for natural gas, the Commission issued Order No. 636,[3] which required pipelines to unbundle their sales and

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[2] Section 2(6) of the NGA, 15 U.S.C. 717a(6), defines a "natural gas company" as a person or corporation "engaged in the transportation of natural gas in interstate commerce, or the sale in interstate commerce of such gas for resale."

[3] 57 Fed. Reg. 13,267, on reh'g, Order No. 636-A, 57 Fed. Reg. 36,128 (1992), aff'd in part and remanded in part *sub nom. United Distrib. Co.* v. *FERC*, 88 F.3d 1105 (D.C. Cir. 1996).

transportation rates. Under Order No. 636, a pipeline generally may act only as a transporter once gas has left the production area and entered the pipeline's mainline systems. See 18 C.F.R. 284.8(a)(1) and 284.9(a)(1). Pursuant to its rate authority under Sections 4 and 5 of the Act, however, the Commission continues to require pipelines that provide gathering services to file their gathering rates. See *Northern Natural*, 929 F.2d at 1265 (Commission has jurisdiction over gathering rates where pipeline itself performs the gathering "in connection with" interstate transportation).[4]

2. Arkla Energy Resources Corporation (now NorAm Transmission Corporation) (NorAm Transmission), an interstate natural gas company, proposed to convey its natural gas gathering facilities to Arkla Gathering Services Company (now NorAm Field Services Corporation) (NorAm Field), its corporate affiliate, which would then assume responsibility for providing the gas gathering services that NorAm Transmission previously had offered. On October 21, 1993, NorAm Field sought from the Commission a declaratory order that certain gathering facilities and services it proposed to acquire from NorAm Transmission would, upon acquisition, be exempt from FERC's NGA jurisdiction. Petitioners, which are producers of natural gas (see Pet. 9 n.7), opposed that request, contending that the Commission was

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[4] The Eighth Circuit observed in *Northern Natural* that "[p]ermitting a pipeline to manipulate the otherwise unregulated charges for gathering services performed over its own facilities in connection with jurisdictional interstate transportation, would, in effect, permit the *pipeline* to establish rates for the interstate transportation." 929 F.2d at 1270.

without authority to disclaim jurisdiction over NorAm Field's gathering rates and services.

The Commission determined that the subject facilities were "gathering facilities" within the meaning of NGA § 1(b), and that NorAm Field, as a provider of services using those gathering facilities (and no other services involving interstate transportation or sales), would not be a "natural gas company" subject to regulation under the NGA so long as it operates its gathering services independently of, and at arms length from, NorAm Transmission's transportation services. Pet. App. 36-103.[5]

The Commission specifically distinguished its disclaimer of jurisdiction over NorAm Field's gathering rates from its assertion of jurisdiction over the

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[5] To insure that the relationship remains arms-length, the Commission directed NorAm Transmission to amend its tariff to add the following standards of conduct:

> (a) [NorAm Transmission] will provide nondiscriminatory access to all sources of supply in accordance with Part 284 of the Commission's regulations and will not give shippers of its gathering affiliate undue preference over shippers of nonaffiliated gatherers or other customers in scheduling, transportation, storage or curtailment priority.
>
> (b) [NorAm Transmission] will not condition or tie its agreement to provide transportation service to an agreement by the producer, customer, end-user, or shipper relating to any service by any gathering affiliate, any services by it on behalf of its gathering affiliate, or any services in which its gathering affiliate is involved.

Pet. App. 63. The Commission also directed NorAm Field to offer gathering-service customers a *pro forma*, or default, contract for gathering services at reasonable rates and terms for a reasonable period of time after transfer of the facilities out of NGA jurisdiction. *Id.* at 64-66.

gathering rates charged by the natural gas company in *Northern Natural*. It pointed out that, while *Northern Natural* involved gathering performed directly by a natural gas company "in connection with" the pipeline's jurisdictional transportation services within the meaning of NGA §§ 4 and 5, this case involved gathering to be performed by an affiliate. The Commission explained that companies (such as NorAm Field) "that perform only a gathering function, whether they are independent or affiliated with an interstate pipeline, are not natural gas companies because they neither transport natural gas in interstate commerce, nor sell such gas in interstate commerce for resale." Pet. App. 61. The Commission took care to emphasize, however, that, while it "generally does not have jurisdiction over affiliated gatherers because affiliates are not natural gas companies," it may disregard corporate form and treat a pipeline and its affiliate as a single entity if the "affiliated gatherer acts in concert with its pipeline affiliate * * * in a manner that frustrates the Commission's effective regulation of the interstate pipeline." *Id.* at 61-62.

On rehearing, the Commission pointed out that natural gas companies often form separate affiliates "for the express purpose of separating the jurisdictional and nonjurisdictional activities," and that, ordinarily, such affiliation does not "subject the nonjurisdictional activities performed by one to the Commission's jurisdiction." Pet. App. 136. At the same time, the Commission again emphasized that it will disregard the corporate form and exert control

over the gathering activities of an affiliated gatherer when "statutory purposes would be frustrated by the corporate form." *Id.* at 138-139 (quoting Opinion No. 255, 37 F.E.R.C. ¶ 61,149, at p. 61,356 (1986)).

3. The court of appeals affirmed FERC's disclaimer of rate jurisdiction over NorAm Field's gathering services.[6] It upheld the Commission's interpretation of Section 1(b) of the NGA, under *Chevron U.S.A. Inc.* v. *NRDC, Inc.*, 467 U.S. 837 (1984), having concluded that "the statute itself does not clearly resolve the question one way or the other," and that "the Commission's interpretation is a permissible resolution of the ambiguity." Pet. App. 15.

The court of appeals rejected (Pet. App. 15-20) petitioners' contention that the Commission's decision conflicts with this Court's decisions narrowly construing the gathering exemption in Section 1(b), *e.g.*, *Phillips Petroleum Co.* v. *Wisconsin*, *supra*; *Interstate Natural Gas Co.* v. *FPC*, 331 U.S. 682 (1947); *Colorado Interstate Gas Co.* v. *FPC*, *supra*. Those decisions, the court observed, "addressed the Commission's jurisdiction over gathering rates charged only by interstate pipelines, and thus do not control the question whether the Commission may regulate rates charged by independent or pipeline-affiliated entities." Pet. App. 15.

The court of appeals also found no conflict between the Commission's ruling here and the Eighth Circuit's decision in *Northern Natural*. Because *Northern Natural* involved the Commission's jurisdiction

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[6] The court reversed the Commission's imposition of the default contract condition on NorAm Transmission (see note 5, *supra*), and remanded that aspect of the Commission's order for further consideration. Pet. App. 33.

to regulate the gathering rates of an interstate pipeline that was itself performing gathering, the court explained that that case "provides no direct support for * * * [petitioners'] claim that the Commission can regulate the gathering activities of [an] independent affiliate." Pet. App. 19. The court noted, moreover, that "the rationale underlying the Eighth Circuit's decision—namely, the perceived danger that unregulated pipeline gathering rates might pose to effective regulation of transportation rates"—was addressed in this case by the Commission's requirement that the "affiliate maintain[] an independent, arms-length relationship with the interstate pipeline." *Ibid.*

Finally, the court noted that the Commission's position—that "an independently operated affiliate, solely providing gathering services, would be exempt from the Commission's NGA §§ 4 & 5 authority to review rates," but that the Commission may "exercise such authority if the affiliate should engage [with the pipeline] in anticompetitive behavior" (Pet. App. 20-21)—"parallels [the Commission's] treatment of gathering in general":

> [W]hile the Commission does not believe it has the general authority to regulate gathering rates, it has never renounced its authority * * * to include gathering costs in the rate base for bundled sales or interstate transportation service. Thus, the Commission consistently maintains that when gathering is intertwined with jurisdictional activities, the Commission's regulation of the latter may necessarily impinge on the former.

Id. at 24. The court distinguished cases, such as *KansOk Partnership*, 73 F.E.R.C. ¶ 61,160, order granting stay in part, 73 F.E.R.C. ¶ 61,293 (1995), clarified, 75 F.E.R.C. ¶ 61,264 (1996); and *Louisiana Gas System, Inc.*, 73 F.E.R.C. ¶ 61,161 (1995), in which FERC had "exercised jurisdiction over chains of interconnected intrastate affiliates that collectively functioned as interstate pipelines," on the ground that NorAm Field will not operate in tandem with NorAm Transmission, but will instead engage solely in nonjurisdictional gathering. Pet. App. 21 n.25.

ARGUMENT

The court of appeals correctly affirmed the Commission's conclusion that its rate jurisdiction under Sections 4 and 5 of the NGA does not extend to gathering services operated by a non-natural gas company affiliate of an interstate pipeline independent of, and at arms length from, the pipeline's interstate sales and transportation services. The court's decision does not conflict with any decision of this Court or of any other federal court of appeals. No further review is warranted.

1. Petitioners argue (Pet. 13-17) that Section 4(a) of the NGA requires the Commission to regulate rates for gathering services performed by an interstate pipeline's affiliate, and that the Commission's decision here amounts to *de facto* deregulation of interstate pipeline gathering rates. That argument is without merit.

Section 4(a) applies by its terms only to "rates and charges * * * received by [a] natural-gas company for or in connection with the transportation or sale of natural gas subject to the jurisdiction of the

Commission." 15 U.S.C. 717c(a).[7] Under Section 2(6), 15 U.S.C. 717a(6), "'[n]atural-gas company' means a person engaged in the transportation of natural gas in interstate commerce, or the sale in interstate commerce of such gas for resale." NorAm Field performs no interstate transportation or sales—only gathering services, which are specifically exempted from the Commission's jurisdiction by Section 1(b), 15 U.S.C. 717(b).[8] Accordingly, under the plain language of the Act, NorAm Field is not subject to the Commission's rate regulation.

Contrary to petitioners' suggestion (Pet. 17), neither *Colorado Interstate* nor *Northern Natural* involved the Commission's jurisdiction *vel non* to regulate a non-natural gas company, like NorAm

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[7] Section 4(a) provides:

> All rates and charges made, demanded, or received by any natural-gas company for or in connection with the transportation or sale of natural gas subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges, shall be just and reasonable, and any such rate or charge that is not just and reasonable is declared to be unlawful.

[8] Section 1(b) provides:

> *The provisions of this chapter* shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use, and to natural-gas companies engaged in such transportation or sale, but *shall not apply* to any other transportation or sale of natural gas or to the local distribution of natural gas or *to the facilities used for such distribution or to the production or gathering of natural gas.*

Emphasis added.

Field, that independently performs only gathering services. Both cases involved the quite different issue of the Commission's authority to regulate the reasonableness of rates charged by natural gas companies that directly engaged in gathering or production "in connection with" their interstate transportation or sale in interstate commerce for resale.[9]

2. The court of appeals correctly found no conflict (Pet. App. 21 n.25) between the Commission's decision in this case and its assertion of jurisdiction in *KansOk* and *Louisiana Gas* over "chains of interconnected intrastate affiliates that collectively functioned as interstate pipelines." The Commission lacks jurisdiction here precisely because the affiliated gatherer and the pipeline do not propose to operate collectively. As petitioners conceded below (Pet. App. 22 n.25), "'[i]t is one thing to argue that a non-jurisdictional affiliate can be created to perform non-jurisdictional activities,' as NorAm Field seeks to do, and 'it is another thing to allow a jurisdictional activity * * * to become a non-jurisdictional activity through the creation of an affiliate,' as the Commis-

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[9] Although the *Northern Natural* court stated in dictum that the expression "gathering facilities owned by the pipeline" includes "such facilities owned or operated directly or indirectly by a pipeline or its * * * affiliate," 929 F.2d at 1263 n.2, the case involved the Commission's jurisdiction to regulate gathering services performed directly by a natural gas company, and the Eighth Circuit held only that the Commission may regulate the rates a natural gas company itself charges for gathering services performed "in connection with" jurisdictional interstate transportation.

sion refused to allow in *KansOk* and *Louisiana Gas.*"[10]

In disclaiming jurisdiction over NorAm Field, the Commission has not, as petitioners charge, engaged in "empty formalism" (Pet. 19) or given "blind deference to corporate formalities in the exercise of its statutory responsibilities" (Pet. 20). Rather, the Commission has correctly recognized that its jurisdiction is limited to natural gas companies, and that companies, like NorAm Field, "that perform only a gathering function, whether they are independent or affiliated with an interstate pipeline, are not natural gas companies." Pet. App. 60-61. At the same time, however, the Commission specifically conditioned its disclaimer of jurisdiction on NorAm Transmission's compliance with substantive standards that imposed upon it an affirmative obligation to operate its jurisdictional services independently and at arms length from NorAm Field. If the pipeline and its affiliate violate those standards and collude so as to effect a jurisdictional service that falls within the Commission's jurisdiction, the Commission is prepared to disregard their separate corporate structures and treat the pipeline and the gatherer as a single entity. Far from giving "blind deference" to corporate formalities, the Commission carefully structured its order to ensure that the affiliated

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[10] For the same reason, there is no conflict (Pet. 20) between the decision in this case and that of the D.C. Circuit in *Altamont Gas Transmission Co.* v. *FERC*, 92 F.2d 1239, 1245 (1996). In that case, the court of appeals merely acknowledged (92 F.3d at 1245), as the Commission did below (Pet. App. 61-62, 138-139), that the Commission may disregard corporate form and "treat as a single entity" a nonjurisdictional gatherer and its affiliated pipeline when the two act in concert.

status of the pipeline and the gatherer cannot be abused to defeat the Commission's jurisdiction over interstate transportation and sales.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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